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STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date:	**06/11/14**	Bill No:	**Assembly Bill 1760**
Tax Program:	**Property**	Author:	**Chau and Bocanegra**
Sponsor:	**Authors**	Code Section:	**RTC Section 214**
Related Bills:	**SB 1203 (Jackson)**	Effective Date:	**01/01/15**

BILL SUMMARY

This bill voids and makes unenforceable a **payment in lieu of taxes (PILOT)** agreement, as defined, entered into on or after January 1, 2015. For PILOT agreements entered into before January 1, 2015, it creates a presumption that payments made under that agreement are used to maintain the affordability of, or reduce rents otherwise necessary for, lower income household occupied units.

Summary of Amendments

Since the previous analysis, the bill was amended to modify provisions related to charges not considered PILOT payments.

ANALYSIS

CURRENT LAW

PILOT Agreements. Existing property tax law is silent on the issue of PILOT agreements related to low-income housing projects.[1]

Property Tax Exemption. The law provides that the welfare exemption applies to certain low-income housing properties. One exemption requirement is that the property owner must be able to certify the following:

- That an enforceable and verifiable agreement exists restricting the development to appropriate lower income household usage and rents.
- That the property tax savings from the exemption are used to maintain the affordability of, or reduce rents otherwise necessary for, the units occupied by lower income households.

The question has been raised whether a property owner can properly make the property tax certification when a PILOT agreement exists with local government. The BOE issued a non-binding legal opinion that a property owner can make the required certification in good faith if rents actually meet or are lower than the restrictions set forth in the enforceable agreement, and if the property owner has a reasonable belief that its PILOT payment will go directly to support or benefit the low-income household units.

PROPOSED LAW

PILOT Agreements. On or after January 1, 2015, this bill prohibits a local government from entering into a PILOT agreement, as defined, with a property owner of a low-income housing project. Any PILOT agreement entered into in violation of these provisions on or after this date is void and unenforceable. "Payment in lieu of taxes agreement" means an agreement between a local government and a property owner of

[1] RTC §237(b) addresses payments that an Indian tribe may make related to a low-income housing project owned and operated by the tribe.

a low-income housing project that requires the owner to pay the local government a "charge" including, but not limited to, any charge designed to compensate for the revenue loss associated with the welfare exemption. A charge does not include any payment made pursuant to a development agreement, as specified[2], that is consistent with prohibitions on discriminatory practices related to residential developments, as specified[3].

Property Tax Exemption. This bill provides that it shall be presumed that any payments made under any PILOT agreement entered into before January 1, 2015 are used to maintain the affordability of, or reduce rents otherwise necessary for, lower income household occupied units.

Refunds and Cancellations. This bill requires any outstanding ad valorem tax, interest, or penalty levied between January 1, 2012, and January 1, 2015, as a result of a PILOT agreement, to be canceled, and any tax, interest, or penalty paid prior to January 1, 2015, to be refunded.

IN GENERAL

Under authority granted by the California Constitution, the Legislature has chosen to exempt from property taxation property used exclusively for religious, hospital, or charitable purposes. The exemption's main provisions, known as the "welfare exemption," are set forth in RTC Section 214(a), which enumerates many eligibility requirements.

In addition to the RTC Section 214(a) requirements, low-income housing projects must meet criteria set forth in RTC Section 214(g). Specifically, under RTC Section 214(g)(2)(B), the low-income housing property owner must certify that:

> [T]he funds that would have been necessary to pay property taxes are used to maintain the affordability of, or reduce rents otherwise necessary for, the units occupied by lower income individuals.

When claimants cannot make this certification, they may not receive a welfare exemption.

BACKGROUND

Recently the Ventura County Assessor's Office sent notification of possible welfare exemption revocation to five nonprofit housing developments that have PILOTs with various cities. The assessor took this action after the office received a courtesy copy of an unannotated December 23, 2011 BOE legal opinion. Based on the particular facts, the legal opinion concluded that the required RTC Section 214(g)(2)(B) certification could not be made with respect to that PILOT agreement. Thereafter, the assessor's office investigated other low-income housing projects with PILOTs, and a statewide discussion commenced to reexamine this issue.

BOE Legal Memo. On March 20, 2013, the BOE's Legal Department issued a memo reviewing this issue, including an earlier annotated letter dated September 29, 2003, (former Property Tax Annotation 880.0155) and concluded that the certification could be made under certain circumstances even when a PILOT agreement was in place.

BOE Town Hall Meeting. On November 6, 2013, the BOE held a panel discussion and some attendees noted the need to pursue legislative action. A video of the town hall

[2] Article 2.5 Development Agreements (commencing with Section 65864) of Chapter 4 of Division 1 of Title 7 of the Government Code.
[3] Government Code 65008(d)(1).

meeting is available online.

BOE Publishes New Annotation. On November 19, 2013, the BOE Members took action to publish a new Annotation 880.0155.005 based on the March 20, 2013 memo and deleted the prior annotated letter.

Property Tax Annotation 880.0155.005 states:

> RTC §214(g)(2)(B) requires a developer to certify that property tax savings be used to "maintain the affordability of" or "reduce rents otherwise necessary for" low-income housing units. A Payment In Lieu of Tax (PILOT) Agreement between a local government and an owner of a low-income housing project does not disqualify a developer from making the certification if rents have been maintained in accord with those required by section 214(g)(2)(A), and the developer has a reasonable belief that the PILOT payment will be used to support or benefit the low-income housing development.

Assembly Joint Informational Hearing. On February 3, 2014, the Assembly Committees on Housing and Community Development, Local Government, and Revenue and Taxation held a hearing entitled "Understanding the Scope of Payment in Lieu of Taxes (PILOTs) and Their Impact on the Welfare Property Tax Exemption." A video of the hearing and agenda is available online via the Cal Channel website.

Legislative Analyst's Office Report. The LAO issued a report for this hearing entitled "Nonprofits and the Property Tax."

COMMENTS

1. **Sponsor and Purpose.** The authors are sponsoring this measure to protect low-income housing developments subject to existing PILOT agreements by creating a presumption that payments made under agreements created before January 1, 2015 support project affordability. The authors state that this bill "addresses the immediate concern facing low-income housing developments with existing PILOT agreements by allowing them to continue receiving the welfare exemption from property taxation and not pay escape assessments. Prospectively, AB 1760 advances the purposes of the welfare exemption by outlawing PILOT agreements going forward."

2. **The June 11, 2014 amendments** modify those charges not considered to be PILOT payments. Specifically, those charges not considered to be PILOT payments, which were previously specified by cross reference to the Mitigation Fee Act, were replaced with a cross reference to charges imposed under the Government Code's Development Agreement laws that are consistent with a Government Code prohibition on discriminatory practices related to residential developments. **The May 28, 2014 amendments** modified those charges not considered to be PILOT payments and deleted a requirement limiting allowable charges to those paid by all other residential developments. **The May 14, 2014 amendments** addressed the disposition of outstanding escape assessments and required the refund of property taxes already paid towards these escape assessments**.** Previously, the bill did not explicitly address escape assessments. The amendments also detailed those charges not considered to be PILOT payments.

3. **PILOT issue simplified.** Low-income housing property may be exempt from property taxation under the Welfare Exemption. Since the local government will not receive its portion of property tax if the property is exempt, low-income housing

developers or owners sometimes enter into agreements (often called PILOT agreements) to compensate local government for costs associated with the property. For property tax purposes, some concern exists regarding the effect of a PILOT on a low-income housing property's eligibility for the Welfare Exemption.

4. **Property tax savings use requirement.** This bill creates a presumption that any payments made under any PILOT agreement entered into before January 1, 2015 are used to maintain the affordability of, or reduce rents otherwise necessary for, the units occupied by lower income households. The purpose of the presumption is to allow the low-income housing developer to make the necessary certification related to the use of property tax savings.
5. **This bill provides legislative guidance that may reduce uncertainty regarding this issue.** The BOE, assessors, local governments, nonprofit organizations, and project financers have an interest in clear and consistent treatment of properties subject to existing PILOT agreements when Welfare Exemption eligibility is at stake.
6. **Financial implications of retroactive property tax exemption revocation.** The low-income housing project owners are very concerned about the prospect of losing the welfare exemption for prior years in which they made PILOT payments. Since they did not anticipate such liabilities, they have insufficient funds to pay back taxes (escape assessments) and associated penalties.
7. **SB 1203 (Jackson) also addresses PILOTs.** SB 1203 eliminates the property tax savings certification.

COST ESTIMATE

The BOE and counties co-administer the welfare exemption. The BOE would incur some minor absorbable costs to inform and advise county assessors, the public, and staff of the law changes and address ongoing implementation issues and questions. These costs are estimated to be under $10,000.

REVENUE ESTIMATE

Information on the number of PILOT agreements has proven difficult to obtain and is unknown, making it impossible to assess the full fiscal impact of this proposal. To date, the identified property tax revenues at stake relate to four low-income housing projects that have received escape assessments for prior years' taxes related to PILOT agreements. Two projects have entered into five-year payment plans and have paid a total of $450,000 toward outstanding liabilities of over $6.1 million. In other projects where PILOT agreements became an issue, the city dropped the PILOT payment requirement to ensure the project would remain eligible for the property tax exemption. Thus, those properties do not impact this revenue estimate.

Exemption eligibility status is uncertain regarding projects located in California, pending the outcome of this issue. The intent of this bill is to maintain eligibility for all projects currently receiving the exemption. This bill will cancel outstanding escape assessments of approximately $5.65 million and refund $450,000 of property taxes paid.

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